# US stocks provide bumper returns

Australian investors in America have been well rewarded

TONY KAYE

New York's Brooklyn Bridge and lower Manhattan bathed in purple light at dusk

Australian investors in US stocks have achieved some spectacular returns over the past year, thanks to the effects of the so-called "Trump bump".

The Dow Jones Industrial Average has gained more than 28 per cent since the election of Donald Trump on November 8 last year, while the technology heavy NASDAQ index is up over 32 per cent.

That's where the biggest US stock gains have been occurring, and where Australian investors including self-managed superannuation fund trustees and members have been most focused.

Although Australian equities investors retain a heavy home bias, preferring the relative safety of the domestic market, a growing number are broadening their portfolio horizons.

Australian Tax Office data shows SMSFs collectively held more than $4.3 billion in overseas shares at June 30, with the US market the favoured destination.

Recent data from software group Class noted that more than 11 per cent of the SMSFs owning international shares have holdings in Apple. A similar percentage hold Alphabet (Google), while Microsoft and Amazon are also among the top holdings.

For those who have ventured offshore, the journey has been very worthwhile in many cases.

Investors in top US stocks such as Amazon and Apple have seen their shares jump by more than 47 and 58 per cent respectively since the US election.

Other technology heavyweights such as Facebook, Alphabet and Netflix, which together with Apple and Amazon are widely referred to as the FAANG stocks, have delivered price returns of between 33 and 60 per cent over the year.

Then there's the electric carmaker and energy storage company Tesla, whose shares have surged close to 70 per cent in 12 months.

Even those who have used the exchange-traded funds on the Australian Securities Exchange to gain access to the US market have done well.

Blackrock's iShares S&P 500 ETF, listed on the ASX under the code IVV, has about $2.3bn in funds under management, while the Vanguard US Total Market Shares ETF (VTS) has about $1.06bn.

IVV units have increased 22.3 per cent over the last year, while VTS units also are up more than 22 per cent.

It's the stuff that share dreams are made of, especially when compared with the mediocre returns by many of Australia's top companies over the same time period.

Our biggest, Commonwealth Bank, has gained about 11.9 per cent, while second on the ladder Westpac has risen a much more modest 4.5 per cent. Telstra, now considerably further down the list of Australia's largest companies than a year ago, has suffered a 29 per cent price fall.

## Will the dollar dazzle investors?

The medium-term returns spread between the top US and Australian companies could become even more pronounced if analysts from the global financial services firm Morgan Stanley are proved right.

They are tipping the Australian dollar is headed for a big fall which, if it eventuates, would provide a massive sugar hit for Australian investors in US stocks.

Over the past year, the Australian dollar has largely flatlined against its US counterpart. On the day of the US election, the Australian dollar closed at US76.1c. Last week, it was at exactly the same level, almost to the fraction of a cent.

That isn't to say it hasn't done anything in between. Just a few days ago it fell to US75.3c, one of its lowest points for this year and, in early September, the cross-rate with the US dollar was at its high point for 2017 to date, at US81.24c.

It's unlikely to be back at that level anytime soon, unless a major political or economic crisis unfolds in the US.

Yet, if an Australian investor had bought into any US stock at the exchange rate peak on September 8, they would be 6.3 per cent ahead now, just from the currency fall.

It's an opportunity lost, for some. Yet, if our dollar does crash, as Morgan Stanley says it will, Australian investors in US stocks stand to be even bigger winners.

The investment bank's London-based chief global currency strategist, Hans Redeker, believes the Australian dollar will slump to an exchange rate of US67c in 2018, and continue slipping to US65c in 2019.

That's based on US interest rates continuing to rise, to the point where the Federal Reserve's cash rate will eventually exceed that of our Reserve Bank's.

As US interest rates rise, more capital will flow from lower-yielding economies such as Australia into those offering better returns.

If the Australian dollar does drop from current levels to US67c, domestic investors in US stocks stand to make almost 12 per cent just from the currency impact alone. Going a step further, a fall to 65c would deliver about 15 per cent — on top of any share price gains produced from the US market itself.

Westpac's chief economist Bill Evans is another who expects the Australian dollar to come under strong pressure over time as a result of both the US-Australian interest rate differential and foreign investor confidence.

"Australia's reliance on foreign investors to fund our large accumulated overseas debt is dependent on offering an attractive yield or a cheaper currency," Evans said last week.

His forecast is that the US official rates will rise above Australia's, with a yield differential of 38 basis points by the end of 2018, and that our cash rate will remain on hold in 2019 as well.

"This sustained period of a negative interest rate differential is expected to take its toll on the $A. By mid-2019 we are looking for the $A to move down to US68c, with the risks pitched to the downside. Overall, around a cumulative US10¢ fall in the $A is expected."

There are never any guarantees in financial markets.

Yet, if the economists are right, and the buoyant forecasts on US technology stocks by some fund managers hold true, Australian investors in US stocks can expect more good upside over the next year and beyond.

*Tony Kaye is the editor of Eureka Report, which is owned by financial services group InvestSMART.*

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DIVIDEND DETECTIVE

# Let Coke add life to your stock portfolio

**Coca-Cola Amatil**
**ASX CODE:** CCL
**SHARE PRICE:** $7.69
**INDUSTRY:** Food and beverages
**FORECAST DIVIDEND:** 46c, 70 per cent franked

DAVID WALKER

Income investors will be wondering if Coca-Cola Amatil's sliding share price makes the stock a buy for yield. At a $7.50 share price, the dividend yield assuming a 46c dividend for 2018 (the current consensus forecast) is 6 per cent — 70 per cent franked. The franking is lower than banks pay but the yield itself is higher than ANZ and CBA, in line with Westpac though lower than NAB. Should the stock be in income portfolios?

The short answer is not yet, but it is time to put Amatil on the watchlist and start thinking about the price you would pay. Most ASX large-caps have rallied nicely over the last year but Amatil stands out for its 20 per cent fall over the same period and its 31 per cent plunge since the stock peaked at $10.87 in April. The stock now trades at a 25 per cent earnings multiple discount to the All Industrials Index ex financials, its deepest ever discount.

This should attract attention because the institutional shareholders of large companies do not tolerate such underperformance for long. Usually there is a catalyst which causes the stock to revert higher. This could be a takeover, a change of directors, management or strategy, or a divestment of underperforming assets.

Amatil is a business in structural decline as Australian consumers switch from carbonated sugary beverages to healthier alternatives. New cola products and smaller pack sizes, bottled water, coffee and alcohol have not so far sufficiently offset this main trend and in the interim result, Australian beverages earnings fell 13 per cent — a problem when Australian operations contribute 58 per cent of group earnings. Cola and mineral water are also particularly competitive categories.

The rollout of container deposit schemes around Australia will further challenge Amatil by increasing compliance costs and raising the retail price of its products, and the company seems unable to quantify the impact at this stage. The stock fell further in recent days after an implied earnings downgrade in 2018 from bringing forward $40m of costs to improve marketing, execution, equipment and digital technology.

*David Walker is ASX large-caps portfolio manager at Clime Asset Management.*

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# Understanding the taxation ramifications of early access to retirement savings

MONICA RULE

You may hear people talk with some optimism about "getting at their super early" — it is possible but there is also a price.

Let me explain.

When a super fund member accesses their superannuation savings, they are usually not aware of how the money is paid from their superannuation fund.

Of course if the superannuation fund is a self-managed superannuation fund (SMSF) and the member is aged 60 or over, it really does not matter as there is no tax payable on the superannuation benefit received by the member.

However, if the SMSF member is under the age of 60, then tax may be payable depending on the amount paid out and the components of their superannuation benefit.

When most SMSF members receive their superannuation benefit it will consist of a tax-free component and a taxable component. The tax-free component represents the personal contributions made into their SMSF where they did not claim tax deductions on the contributions.

The taxable component is made up of contributions such as employer contributions, salary sacrificed contributions, personal contributions where tax deductions have been claimed and investment earnings received by the SMSF. The SMSF would have paid a maximum tax of 15 per cent on this money and when the money is paid out to the member, as a superannuation benefit, it is represented as a taxable component.

Now, if an SMSF member's superannuation savings does consist of tax-free and taxable components, unfortunately they cannot just choose to access their tax-free component.

Under the taxation law, all money withdrawn from a superannuation fund must be paid in the same tax free and taxable proportions as they exist in the fund.

This means, if an SMSF member's accumulation account has 20 per cent tax free money and 80 per cent taxable money, then their lump sum superannuation benefit must be paid out in the same percentages.

For example, if a member withdraws a lump sum super benefit of $300,000, then $60,000 would be the tax free component and $240,000 would be the taxable component. Of course it should go without saying that the member should only access their superannuation savings if they have met a condition of release under the superannuation law.

There is no tax payable on the tax free component regardless of the age of the member receiving the lump sum benefit. However, if the member has not reached their preservation age when accessing the money, then tax is payable at a maximum of 20 per cent plus the Medicare Levy on the taxable component. If the member has reached their preservation age but is under the age of 60, then the first $200,000 (that is, low rate cap for 2017-18) is tax free and the balance of the money is taxed at maximum of 15 per cent plus the Medicare Levy.

Of course if the SMSF member is aged 60 or over, then no tax is payable on both the tax free and taxable components.

The same rule applies to members commencing an account-based pension from their SMSF. The tax-free and taxable components are determined at the commencement of their pension. The percentages remain the same throughout the duration of the pension. Each time a pension benefit is paid from their SMSF, it is paid in the same percentages.

Understanding the treatment of superannuation will assist you with decisions when accessing your savings.

*Monica Rule is an SMSF specialist and author of The Self Managed Super Handbook — Superannuation Law for SMSFs in Plain English.*

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